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FATHER~SON

agreements for operating farms



FARMERS' BULLETIN NO. 2179
U.S. DEPARTMENT OF AGRICULTURE

Father-son farm agreements are of two general kinds: (1) Farm-operating agreements and (2) farm-transfer agreements. This bulletin deals with farm-operating agreements only.

A transfer agreement sets up a definite arrangement for transferring part or full ownership of the farm to the son at some specified time. Because such an agreement involves all members of the family it should be considered a family farm-transfer agreement.

Readers may wish to inquire elsewhere about farm-transfer agreements. Several State colleges of agriculture have bulletins on this subject. Another possible source of information is the county agricultural agent.

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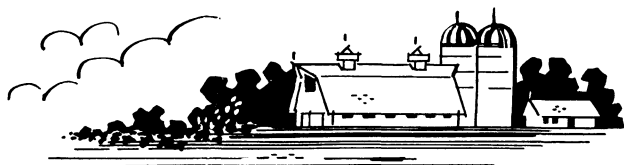
Prepared by

ECONOMIC RESEARCH SERVICE

This bulletin is a revision of, and supersedes, Farmers' Bulletin No. 2026, "Father-Son Farm-Operating Agreements," by Max M. Tharp and Harold H. Ellis, issued in 1951. This revision is largely a condensation of the earlier bulletin, except for tax information, which reflects recent changes in the law.

WASHINGTON, D.C.

Issued December 1961
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FATHER-SON *agreements for operating farms*

A well-planned farm-operating agreement between father and son has many advantages. The nature and scope of the advantages vary with the kind of agreement.

In general, such an agreement makes it possible for a young man to get capital quickly—by beginning farming on an established farm that calls for and rewards his best efforts. For the father, it may offer a solution to the problem of retirement—by allowing him to curtail his hard work while retaining an interest in a business it has taken him years to build.

Many farms are likely to run down when the farmer grows older; bringing a younger man into the business often can keep production at a high level. At the same time, the older man's experience and understanding helps to keep the farm organization stable.

Agreements similar to father-son farm-operating agreements may be entered into by other relatives or by others who want to operate farms on a similar basis. The large amount of capital needed to start farming nowadays may make this practice more and more desirable.

KINDS OF AGREEMENTS

Two kinds of agreements—project and enterprise—are ordinarily apprenticeship arrangements.

The two usual kinds of agreements for full-time operation of a farm are: Wage and income-sharing and joint operation.

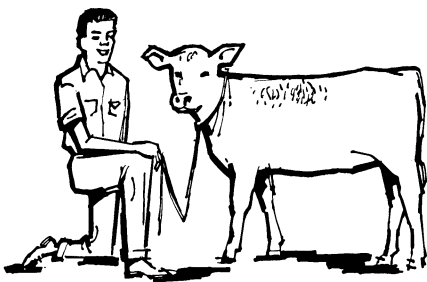
Project and Enterprise Agreements

Project agreements usually are informal. They start while the son is young. Such an agreement may start when the father gives his son a calf, a pig, or some chickens; puts him in charge of the garden; or makes him

responsible for growing all or part of some minor crop. Or the agreement may begin with a 4-H Club or vocational agriculture project.

The logical next step is to let the son be responsible for an enterprise. At first he might take on only a single enterprise suited to the amount of time he can give to it—the poultry flock, the dairy, or a tobacco crop, for example.

The share of the income the son receives from his enterprise may be based partly on the labor, management, and capital he puts into it. He should be encouraged to develop a herd or flock,



or to invest his earnings in machinery or other equipment. This should lead to a gradual accumulation of capital in either property or money.

During this time also the son will be developing skill in management and in getting practical farm business training. From this kind of agreement, father and son may look forward to the time when they will be joint owners of the whole farm, or when the son can begin on a farm of his own.

In most cases, project and enterprise agreements should be considered as leading to something more. They do not develop a well-rounded interest or skill in all phases of farm management.

Wage and Income-Sharing Agreements

A wage and income-sharing agreement is a good temporary arrangement. Under this kind of agreement the son is paid a wage—usually monthly—plus a share in the net farm income. Part of this share of the income might be paid to him in the form of certain livestock, machinery, or other equipment.

This kind of agreement might be used when the son returns home after an absence of several years—in the Armed Forces, at college, or working off the farm. During the time the agreement is in force he and his father

can find out whether his interest lies in farming.

This kind of agreement may also be used when a married son returns to the farm. He may need the cash from wages for living expenses.

Under a wage and income-sharing agreement, the son has a special reason to work steadily and to take the point of view of a manager rather than of a hired hand. Because of his interest in having the profits as high as possible, he is likely to do his best to keep costs down, as well as to increase the total income. As a result, the net income to both father and son may be increased.

The legal relationship between father and son under a wage agreement is usually that of employer and employee.

As an employee, the son is not responsible for the liabilities and losses of the business. On the other hand, he has authority to do only the things that the father authorizes him to do.

The father, under such an agreement, is liable for the son's torts committed in the course of employment (a tort is any wrongdoing in the eyes of the law other than a crime or breach of contract). The father can take out insurance against such liability.

Joint-Operation Agreements

When the son has had experience and is ready to devote full time to farming, an agreement for joint operation may best fit the situation. Such an agreement provides for joint management and control by father and son. The types of legal agreements or enterprises they may enter into include partnerships, leases, and corporations.

Ordinarily, in the beginning stages of a joint-operation agreement, the father continues to own the real estate. He may receive interest on his invest-

ment in the land according to its estimated value. Or he may receive an agreed rental for the farm.

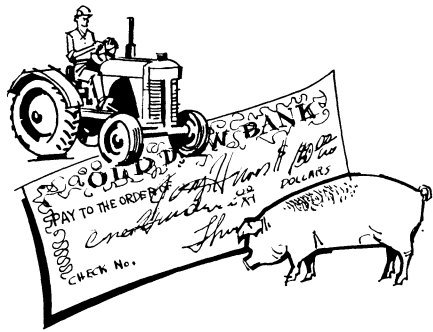
In either case, if the father is paid for the use of the real estate he is expected to pay the taxes, the upkeep, and other expenses on the land and buildings. Generally, increases and decreases in inventories of livestock, machinery, and other operating equipment are shared in the same proportion as the income.

If the father can afford to do so, he may contribute his real estate at a nominal figure to help build up the son's share of farm income. If the farm is free of debt, this would not cost him any cash; he would merely forgo the interest return or rent from his investment, and the son would probably be expected to pay part of the taxes and other cash expenses on the real estate.

The sharing of ownership and income may be in any proportion that is satisfactory to both. A rough approximation for sharing income may be worked out by making the share each receives proportional to the amount he contributes.

For example, if the value of the son's contributions in the form of capital, operating expenses, labor, and management equals 50 percent of the total contributions, then he would receive 50 percent of the farm income. This method of figuring is often used by landlords and tenants in determining the rent to be paid for a farm. The method should be varied to suit individual needs and wishes. A father may want to give his son a better deal than is customary in farm leasing.

Some of the agreements provide for dividing the net farm income on a profit-sharing basis. Under this scheme, each person is paid for what he contributes to the farm business. Then, when the value of all contributions and the farm expenses have been



deducted, the remainder is divided between father and son according to the percentage agreed on.

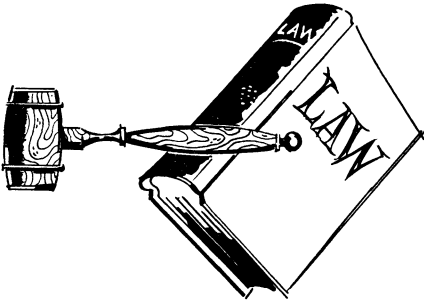
Agreements for joint operation represent a mature stage in father-son operation of the farm. Usually they are drawn up after the son is old enough to have gained valuable experience and to have saved some money to invest in the business. Usually his regular schooling has been completed and he can spend full time on the farm and take over a larger part of the management.

By this time, too, the father may have reached the age when he wants to "slow down and take things easy." Joint-operation agreements pave the way for passing the responsibility for management and actual farming to the younger generation.

Partnership agreements

By the time the agreement has advanced to the joint-operation stage, father and son may want to form a partnership.

Partnerships make possible the equal sharing of profits and losses and equal participation in management and operation. Each partner can contribute property to the business, and joint (undivided) ownership of property can be maintained. The partnership may acquire title to personal property and, in many States, to real property.



Legal consequences.—Certain legal consequences of a partnership should be carefully considered.

Each partner is the agent or representative of the other in carrying on business in the usual way. He can go into debt, make contracts, and buy or sell partnership crops, livestock, and other property without the consent of the other partner. A minor may disclaim personal liability at any time before or upon coming of age. But, in most States, he cannot prevent partnership assets from being held liable.

Each partner (with the exception of minors in some States) may be held liable to third persons for any torts committed in the course of the business by the other partner or by partnership employees.

Farmers' Comprehensive Personal Liability Insurance may be used as protection against most of this liability. This type of insurance policy usually contains certain exceptions relating to the operation of motor vehicles; automobile, truck, tractor, and implement liability insurance can give protection to cover these exceptions.

Under certain circumstances, each partner may be held liable for injuries to partnership employees. They may jointly take out Employers' Liability or Workmen's Compensation Insurance against this risk.

Even though, in most States, a farmer is not required to take workmen's compensation insurance, he can usually

obtain such insurance as an addition to an employer's liability policy. Under this "voluntary compensation endorsement," compensation benefits are provided to workers in addition to the liability protection given to the employer.

If the partners are engaged in a recreational business like hunting, boating, or horseback riding, they can obtain a special endorsement to the Farmers' Comprehensive Personal Liability Insurance Policy to protect themselves against the liability risks associated with these activities. Alternatively, an Owners', Landlords' and Tenants' Policy can be used that provides liability coverage for nonfarm business activities.

Personal property contributed to the partnership business ordinarily becomes partnership property, unless it has been otherwise agreed. Therefore, a partner who wants to retain exclusive ownership of the personal property he contributes should be sure there is a written and signed partnership agreement that provides that he is contributing only the "use" of the property. This agreement may be especially important if one partner should die while the partnership is in force.

If one partner dies and the partnership agreement does not provide otherwise, the surviving partner may have to settle the business immediately.

Property held in partnership may have to be sold and the proceeds distributed in cash if so demanded by the surviving partner or the deceased partner's legal representative. Suggested provisions that may be included in an agreement to avoid such consequences are listed on page 5.

Restrictions on the partners.—The partners may agree to restrict the authority of each to incur obligations on behalf of the other. For example, they may agree that neither can make cash purchases or sales that involve

more than a specified amount without mutual consent; or that neither can borrow money, enter into contracts, or make purchases on credit, without the other's written consent. These restrictions, however, protect the partners only against third persons who have been told about them. Therefore, it may be a good idea to tell persons with whom the partners expect to do business about the restrictions that have been agreed on. Avoiding a joint checking account or limiting the use of one (such as requiring the signatures of both partners) will make such restrictions more effective.

Avoiding formation of a partnership.—If father and son jointly participate in the operation of the farm business on an equal managerial basis, and share in its profits, it may be hard to avoid forming a partnership.

Avoiding a partnership will be even more difficult if both have invested capital in the business, or if they have a joint bank account, or if much of the property used in the business is owned jointly rather than separately. These are all earmarks of a partnership.

Because of differences in court decisions, it may be easier to avoid a partnership in one State than in another. Chances of preventing formation of a partnership may be improved by drawing up a written agreement in the form of a lease, if the father owns the farm, and including an express disclaimer of a partnership together with a denial of any authority of one to act for the other. But ordinarily, such a disclaimer will not guarantee that a partnership can be avoided, so it may be a good idea to guard against partnership liabilities even though what is considered a nonpartnership arrangement has been drawn up.

Family farm corporations

Farm businesses may be incorporated in all States. But, as of 1966, in

Kansas there are certain restrictions including limitations on the numbers of stockholders and acres controlled and a residency requirement. In North Dakota, only cooperative farming corporations may be formed and 75 percent of the members or stockholders must be farmers residing on farms or depending principally upon farming for their livelihood.

Farm corporations are not numerous. However, the number of incorporated farms in some States has increased substantially in recent years.

The corporate form has been used principally by larger family farm businesses. Ownership interests in the corporation (shares of stock) generally are limited to members of the family and are not available for public purchase.

Farmers who incorporate frequently seek advantages—such as limited liability, ease of transferring property interests within and between generations by stock transfer, easier continuation of the business after death of the original owners, income tax saving, and more flexible retirement planning. The ease of sharing income and expenses proportionately under the corporate form is an additional reason for incorporating.

The corporate form may be a useful device for the organization of a hybrid seed business, orchard, or retail milk route. For such enterprises the corporate characteristic of continuity of life may be helpful in retaining the goodwill and going-concern value of the business. Recent changes in the Federal income tax law also make incorporation attractive for many family farms that formerly did not consider incorporation feasible.

Legal advice is needed to organize a corporation. Written articles of incorporation and perhaps other relevant information must be supplied to the State before a charter can be obtained.

Organizing and carrying on a corporation involves considerable paper work. In addition to articles of incorporation, by-laws ordinarily should be drawn up. An annual report must be made to the State and any issuance of stock or alteration of the corporate capital structure may have to be reported. Usually, an annual stockholders' meeting must be held. There generally must be at least three incorporators and three directors (an incorporator may also be a director).

The liability of members of a corporation (stockholders) for corporate obligations usually is limited to their capital investment plus their share of undistributed profits. When a father and son are engaged in farming, however, the capital invested by each (especially by the son) may represent his total assets.

Stock certificates are evidence of ownership in a corporation. They provide a clear record of each stockholder's proportionate rights in corporate assets and profits. They do not help, however, to distinguish corporate property from the separate property of father and son.

Death of a stockholder or other changes in membership need not affect the life of the corporation; in most States it may continue indefinitely. But if the corporation is dissolved, this may require reports to the State, payment of obligations to creditors, and distribution of cash or corporate property to the shareholders. There also may be some additional income tax liability for the shareholders.

Lease agreements

A farm-lease agreement may best fit the situation when the father does not want to continue taking an active part in the management and work of the farm.

Under a farm-lease agreement, the operator (son) usually provides all or most of the labor and management and often supplies all or part of the equipment as well. If the farm is operated under the usual cash or crop-share lease, the father would ordinarily exercise little management control over the farming carried on by the son as a tenant. In some livestock-share leases, however, the landlord (father) may take part in some of the management decisions and may still own part of the livestock and equipment.

Generally, neither landlord nor tenant may bind the other, without consent, by incurring debts, entering into contracts, or selling farm products or other property in which both have an interest. Nor is either party usually liable for any torts committed by the other under the landlord-tenant relationship. But if either authorizes the other to do certain things on his behalf he may be held liable for any torts committed by the other while acting under the authorization. Most tort liability, however, may be covered by insurance.

In some livestock-share leases the business relationship of father and son closely resembles a partnership. In addition to providing the farm, the father has a part in the day-to-day management decisions, owns a share of the livestock and operating equipment, and may also contribute his labor to the business. Under this arrangement it may be hard to determine whether the courts in deciding a particular question would regard the agreement as a partnership, a lease, or both. Courts are less likely to regard such arrangements as partnerships in some States than in others.

See page 5 for discussion of factors that may help to avoid a partnership

and precautions that may be taken in regard to partnership liabilities.

If the father and son decide that they will enter into a leasing arrangement, they may find it helpful to use lease forms (and guides for filling out the forms) issued by the U.S. Department of Agriculture. The forms, and guides to assist in using them, are: the "Crop-Share-Cash Farm Lease" (AD 561) and "Your Crop-Share-Cash Farm Lease," Miscellaneous Publication 838; the "Cash Farm Lease" (AD 562) and "Your Cash Farm Lease," Miscellane-

ous Publication 836; and the "Livestock-Share Farm Lease" (AD 563) and "Your Livestock-Share Farm Lease," Miscellaneous Publication 837. The "Annual Supplement to Farm Lease" (AD 564) can be used to record changes in the lease agreement. "Your Farm Lease Checklist," Farmers' Bulletin 2163 can be used to determine if essential points have been included in the lease.

For a listing of other publications about leasing and directions for obtaining copies of them, see pages 17 and 18.

PLANNING FOR SUCCESS

Three factors have a great deal to do with success or failure of any father-son farm-operating agreement. They are:

- Capability of the farm.
- Cooperativeness of father and son and other family members involved.
- Suitability of housing for a second family, if necessary.

The Farm

Not all farms are suitable for the development of father-son operating agreements. Some are too small; some are not productive enough; some are so poorly organized that they cannot support two families; some are so located that they cannot be made into the kind of unit upon which a son wants to spend his life and rear a family.

Many of these unsuitable farms can be adapted to father-son operation by the adoption of certain plans to increase the size or to change the organization.

Size.—Most farms with father-son operating agreements are larger than the average for their community.

If a farm business as now organized is too small to provide a satisfactory income for two families it may be possible with the son's help to reorganize and enlarge it. A usual way to make the business larger is to rent or buy additional land if land is available for rent or if sufficient capital or credit is available to permit buying land.

Sometimes the size of the business can be increased without increasing the size of the farm—by using more labor and capital. Enterprises that use more labor (such as dairying) may be added or increased in size and the additional capital invested in such items as more fertilizer, better seed, or improved breeding stock. More land may be made available for use through drainage, clearing, or irrigation.



Adding certain livestock enterprises to the farm often brings about a better use of labor. These additions require capital. But if the full-time agreement has grown from a project or enterprise arrangement the son may already have the animals that will form the basis of a herd. This method of changing the farm organization to fit the increasing need for income, as the son takes a greater part in the business, should be kept in mind as plans develop. "Growing into" a new enterprise is often better than "buying in."

Sometimes the size of business may be increased by increasing the number of processes carried out on the farm or by furnishing more services than are usually provided. For example, a shift might be made from the sale of milk for manufacturing to sale of Grade A milk. Or eggs, vegetables, fruits, or other products might be packaged on the farm and sold at retail.

Type.—Certain types of farms may be better suited to father-son operation than others. Dairy farms, for example, may be better suited to this type of operation than cash-crop farms. It may be more difficult to lead into a lease or a partnership on a cash-grain farm than on a livestock farm.

On livestock farms, agreements can be made that lead to joint operation or full partnerships. The boy who starts with a heifer or a sow can build up a herd within a few years. A son on a cash-grain farm may not have equal chances to see his money grow, as he ordinarily would invest his savings in machinery and equipment.

Mortgaged farms.—Establishing a full-time father-son operating agreement is easiest if the farm is not heavily indebted. Many fathers and sons have worked out successful agreements on mortgaged farms or on farms being purchased under a land contract, but

principal and interest payments complicate the agreement. They must be paid in cash and they become a farm expense. Because the retirement of the debt and payments of interest must be made regularly, the farm will have to return enough income to carry this expense. This fact should be considered when plans are made for joint operation.

If interest and principal on the debt are paid from joint earnings, special recognition of the son's contribution to retirement of the debt should be made. He may be considered as buying a share in the real estate when he helps to pay off the debt. An understanding of the amount to be paid by him and the method by which he is to be compensated should be reached, put in writing, and signed. When the debt is fully paid the father may want to give the son a deed or make a binding contract to show to what extent he has bought into the farm.

Unless the son has something in writing, signed by his father, to show his contribution to the retirement of the debt, his investment may be lost at his father's death, particularly if there are other children to share in the estate. Several ways of compensating the son are possible. A lawyer could help arrange a satisfactory method.

Rented farms.—Father-son agreements may be used successfully on rented farms if the size of the business is adequate and the income is sufficient to pay the rent and furnish a living for the families of both father and son.

The agreement between father and son on a rented farm could give the son the same chance to get experience in managing and operating that would be possible if his father owned the farm. This would depend on the rental agreement with the landlord.

Although the opportunities to accumulate capital on a rented farm may be

limited, a way can usually be found for the boy to own some livestock, machinery, or other operating capital. The object of the agreement may be to help him get a farm of his own, or to help father and son to purchase a farm jointly.

The Family

For a successful agreement the father must be sufficiently wise and open-minded to recognize the son's maturity and increasing ability. The son must have confidence in, and respect for, his father. The attitude of the mother and of the son's wife are also important; unless the younger woman likes farm life and has a real interest in the farm business, an agreement is not likely to work out well.

Father-son farm-operating agreements are easier to start when there is only one son or only one who is interested in working the home farm. Most parents want to treat all their children equally. The son who farms with the father sometimes may be regarded by the other children as getting more than his share, especially if there is also a transfer agreement providing that he is eventually to own part of the real property.

Farms operated under a father-son agreement offer good opportunities to maintain or increase farm production. Often, because it is an agreement between members of family, both invest willingly in production items and in other items that increase the longer term productivity of the farm. They may do this with the expectation that the agreement will continue and both will be able to obtain the full return on their investment.

Special consideration needs to be given to the contributions made by a son if there are other children. They

may not realize that the value of the farm has been increased by such contributions of the operating son as building repairs, and soil conservation structures and other land improvements.

In preparing a farm-operating agreement, attention should be given to social security benefits and taxes. For employees and self-employed persons in agriculture who meet the requirements, the program is compulsory. However, the type of arrangement may affect the way the father and son are treated in the program.

Since, up to a point, benefits increase as taxes increase, father and son may want to adjust the division of farm income and the form of income (such as wages, rent, or shares of farm receipts) to take fullest advantage of the social security program. In deciding on a type of operating agreement, the father and son should take into account the effect of social security on the current and future income of both.

In general, rental income is not taxable for social security purposes nor is it deductible from benefit payments received—it is not considered earned income. However, if the landlord participates materially in the farm operation, the entire rental income may be considered earned income and it is taxable and must be deducted from benefit payments. If the father and son are considered operating partners for social security purposes, then both their incomes are subject to the social security tax.

When there are two or three sons who want to farm they might all be brought into the business if it is, or can be made, big enough to accommodate them all. This might be done by renting or buying additional land. Very often, however, this cannot be done, either because it is not possible to enlarge the farm sufficiently to support

several families or for other reasons. The oldest son might accumulate enough capital and equipment, through taking part in an operating agreement, to start on another farm by the time a second son is ready to work full time with his father.

If the boy who leaves the home farm can rent or buy in the community his father may be able to help him in ways that do not involve the expenditure of cash. They might exchange work in haying, corn picking, or tobacco harvesting and might lend equipment to each other.

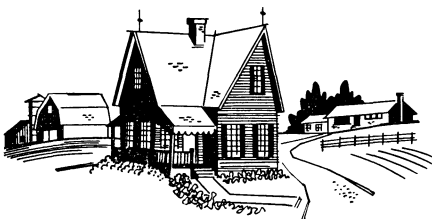
Housing

The chances for success on a jointly operated farm are greater when each family has its own living quarters.

Remodeled house.—If there is a tenant house on the farm it might be remodeled to provide separate living quarters for one of the families. Or possibly a garage or some other farm building could be remodeled.

New house.—If the farm is large enough to need two men for efficient long-time operation, it might be wise to build a new house.

The new house should be situated so that it will be convenient for doing the usual farm chores, but not too close to the older house. If the farm is to be divided sometime in the future, the new house should be located accordingly.



In deciding which family is to occupy the new living quarters, consider the particular housing needs of each family. Perhaps a smaller compact house would suit the parents. Meanwhile the son and his wife may need the larger old house, particularly if they have a growing family.

If the son pays part of the cost of building a new house, his interest should be protected. This might be done by selling or otherwise transferring to him the house and tract of land on which the house is built.

Rented house.—Another possibility is a rented house. This might be a house on another farm in the community or in a nearby town.

If an additional house is rented for either family, responsibility for payment of rent must be agreed upon in advance. As joint operators, both may be entitled to receive their living quarters from the farm business. So the rent on the additional house might be paid out of the undivided farm income. This decision, however, will depend upon individual circumstances.

Apartment.—If the farmhouse is large enough it might be converted into two separate apartments. This arrangement may be particularly desirable when parents need a younger person near. If this plan is put into effect it is usually well to have the apartments entirely separate, with separate entrances, kitchens, and bathrooms—especially when the son has young children who might disturb the older couple.

Buying a house and moving it.—It is sometimes possible to buy a house and have it moved to the farm. This provides a good solution to housing problems when it is desirable for both families to live on the farm and it is not feasible to build a new house or to remodel the farmhouse.

DECISIONS TO MAKE

Before having an agreement drawn up father and son must settle four big questions, among others—

Exactly what will each contribute to the business?

How will increases and decreases in inventory be shared?

How will operating expenses and receipts be shared?

How will finances be managed and records be kept?

Father and son should think about and discuss these matters. If necessary, they should talk them over with their county agricultural agent or some other person who can give technical assistance.

They might be interested in referring to some of the publications listed at the end of this publication. In particular, Farmers' Bulletin 2162, "Your Farm Rent Determination Problem," may be useful in helping them to reach agreement on such questions.

Contributions to the Business

Good business methods indicate that a value should be put upon each contribution to the farm business. The main contributions are of real estate, personal property, labor, and management.

In the early stages of the agreement, the son may have only his labor to contribute. As he accumulates some capital and gains experience, he can contribute more. As his contributions increase, his share of the farm income should increase proportionately.

Real estate.—The father usually is in a better position to furnish the real estate—even after the son is participating full time as a joint operator in the business. If the land is rented, the son as a joint operator should contribute



his proportionate share to the rental, either in cash or a share of the crops.

One way to estimate the value of land and buildings is to base the value on the long-time earning capacity of the farm. The interest rate charged on this earning-capacity value might be the current rate on long-time mortgage loans. This method of estimating eliminates any wide fluctuations in contributions caused by changes in price of land. Another way of valuing the real estate contribution is to use the rental rate for comparable land in the community.

If the father, as owner of the land, pays the costs for new buildings or other major improvements, the valuation of his contribution of real estate should be adjusted accordingly. If the son pays part of the costs an arrangement should be made to protect his investment if the agreement is terminated.

Parents who own their farm may want to furnish the land and buildings without requiring any rental or interest payments and simply receive a share of the profits. If this is done, the cash costs of ownership—taxes, insurance, and maintenance expense—can be shared.

But as owner of the land and buildings the father could receive a return from their use in the form of interest on the investment, or rent. If he receives rent for real estate, he may be

expected to pay taxes, insurance, upkeep, and other expenses on land and buildings.

If the farm is mortgaged the interest charge is a cash expense which may be paid by the father from his return on investment, or from joint earnings. But if the farm is free of debt the investment charge for use of real estate may not be regarded as a cash cost.

Personal property.—In the early phases of an agreement the father may furnish all or nearly all of the personal property. If it is agreed that the son should receive a substantial share of the profits of the farm business even though he does not own much of the personal property he may want to buy a part interest from his father to make up the difference.

Sometimes fathers sell an interest in the livestock, machinery, or other personal property to their sons and take notes for the debt. The son then usually pays interest on the note and retires the principal from his share of farm earnings. He thus becomes a joint operator earlier than if he had had to save the entire amount before going into business.

Under certain circumstances some fathers agree to give their sons a half interest in the personal property when the full-time agreement begins. Others take a non-interest-bearing note. Generally anything that is mutually agreeable between parents and children can be worked out.

An inventory of all personal property should be taken when the full-time agreement begins. It should include all livestock, machinery, equipment, feeds, and supplies. A monetary value should be placed on each item and a record of ownership should be kept. Written evidence of ownership interest is especially important when either party dies.

Labor.—Usually both father and son contribute their labor to the farm business. The estimated value of labor should be decided according to the particular current situation. The customary rate for hired labor in the community can be used in making the estimate.

Whether to use the prevailing wage rates or a long-time average should be decided. The decision made might depend on the basis that is used in valuing real estate. If long-time earning-capacity values were used to value real estate it might be appropriate to use a long-time average wage rate.

If it should become necessary or desirable for one of the joint operators to work off the farm part or full time it is usually best that the father do this. This may fit into his plan to take things easier by turning over more of the farming to his son. If either father or son works off the farm part of the time, his labor contribution to the farm business is likely to be decreased; if so, adjustments can be made from time to time to fit changing conditions.

Management.—Evaluating management is not easy. Perhaps it usually would be best to assume that management is contributed jointly by father and son and to make no attempt to put a money value on it. The idea is for the son to take a substantial part in the management of the farm as confidence is built up under the patient guidance of the father.

Often the son has learned of new developments in agriculture through his high school or college work, or through his reading, or at meetings. He may be acquainted with new farming practices, improved varieties of crops, new kinds of seed, new ways of using fertilizer, and improved livestock rations. The father should let him try

new methods and new ideas, but guide him in following a reasonable course.

Ownership in Inventory Changes

Increases and decreases in the inventory value of personal property are usually shared in the same proportion as ownership is shared. If all the land belongs to the father, increases and decreases in its value are generally his.

The son may help to make improvements to the land or buildings or pay part of the costs of new buildings and fences. Over several years the productivity of the farm may be built up by adopting soil-conservation practices and measures, adding fertilizer, and developing pastures. When the son has helped to make such improvements his investment should be recognized and protected.

Careful records should be kept to show the contributions made by the son to improve land owned by the father. An agreement should be reached, put in writing, and signed, specifying how the son is to be compensated for these contributions. It is sometimes advisable to transfer to the son a share in ownership of the real estate because other children in the family may be inclined to disregard or to underestimate the value of improvements that the son has helped to bring about.

One of the following may be used as a basis for determining the value of the son's contribution to real estate improvements:

- The cost of the improvement according to a detailed record of expenditures; the son's labor should be considered in calculating this cost.
- The replacement cost according to an appraisal at the time settlement is made.
- The depreciated value as determined in income tax reports.
- The added value at the end of each year. This would be an estimate of the value of the improvement to an incoming operator.

Operating Expenses and Farm Receipts

In the early stage of an agreement, the son may be allowed to keep all the income from his project or minor enterprise, especially if he has paid the cash expenses connected with it. Expenses that are not in cash—such as use of barn or pasture for a cow and calf—may often be furnished by the father without cost.

On a crop project the father may share in the receipts if he prepares the land, buys the fertilizer, or pays other cash expenses. How receipts are shared depends upon what the father thinks will give his son the kind of experience, training, and incentive he needs to develop into a full-time partner.

The expenses will usually be shared in a full-time joint operation. The part paid by the son will depend upon the circumstances and the wishes of father and son. Usually, important purchases and sales are made only after they talk them over together. Either, or both, may be empowered to pay the regular operating expenses. To avoid misunderstanding later they should agree in advance to the method to be followed.

Arrangements may be made for making regular withdrawals from business income to meet personal expenses. These withdrawals may be regarded as payments for labor at a specified monthly or weekly rate, or they may be a flat sum to cover living expenses. An agreement should be reached on the

amount of money to be taken out regularly. Too many agreements fail to specify how family living expenses are to be met, and the son has to ask for money he needs. The son should not have to ask his father for money he has earned.

Managing Finances

How the farm finances are to be managed should be definitely understood between father and son. Too many agreements drift along from projects to full-time joint operation with no definite plan for handling accounts. Father and son "just farm together." Operating and living expenses are paid from the father's account and any surplus goes back into the business. Although an agreement can be successful under these circumstances the chances for harmonious, continuous operation are greater if there is a businesslike mutual understanding regarding finances.

A joint bank account in which all farm receipts are deposited and from which all expenses are paid may be an aid to good management. (But, as noted earlier, avoiding such an account may help in avoiding a legal partnership.) In addition to the joint account, each may want his own account for personal finances. If a joint account is used, each might draw a monthly or weekly allowance from the joint account and deposit it in his personal account.

Some fathers and sons maintain separate bank accounts—but no joint account. They divide the main receipts and expenses as they go along and settle at regular intervals for minor items paid or received by each.

Any well-organized farm business has a set of written records. These may include an itemized account of receipts and expenses (including capital

outlays), a property list or inventory, and an account of production.

A simple yet complete set of farm records provides a basis for a yearly settlement and supplies the information and evidence needed in filing income tax returns. A good set of records also serves as a guide for improving the efficiency of the farm operations.

All farm-operating expenses and such fixed expenses as taxes, interest, and insurance, as well as all farm income from sales, customwork, or any other source, should be itemized in the farm records.

The records should also include a detailed inventory of all farm property at the beginning of the agreement; at settlement time, it should reflect any changes in inventories of livestock, feed, equipment, and other personal property as well as improvements made in real estate. The amounts paid and received by each party should be clearly indicated, and the ownership should be shown for all property—real estate, livestock, machinery, equipment, feeds and supplies, and any other property used in the business.

Any income or expense that is not to be shared should be noted. This will help to avoid misunderstanding at settlement time. The farm accounts should be settled at least once a year and in some cases monthly settlements may be desirable. The final settlement should come at the same time each year. A decision should be made on the way in which any surplus or loss is to be handled.

In addition to the cash accounting and settlement, inventories should be brought up to date. All property should be listed and the ownership interests of father and son clearly indicated.

Annual or more frequent reviews of the finances and progress of the farm business are also helpful.

DRAWING UP THE AGREEMENT

Whether they cover a few details of the operation or many, farm-operating agreements should be written.

Putting the agreement in writing has many advantages. It helps to prevent misunderstandings. It puts the arrangement on a businesslike basis. Many oral agreements are indefinite and leave decisions to be made from day to day as each question comes up. If the agreement is written, the problems and terms will be more thoroughly discussed than if it is oral. This discussion helps father and son to agree upon details and to have a clear understanding of the agreement.

Agreements about shares in real estate generally must be in writing and signed to be legally enforceable. In many States, this may be true for any agreement that is to last for a definite period longer than a year.

A written agreement gives evidence of the son's part in the management and operation of the farm. It should be complete, yet fairly simple—with the provisions clearly stated. It should be reviewed from time to time and changed if necessary.

Operating details.—A father-son agreement usually covers all essential operating details of the business. These include contributions of both father and son—of labor, management, capital (real estate and operating), and expenses. Provisions for maintaining the farm and sharing in new investments and in farm receipts are generally included.

Fathers and sons who are working out such agreements should be aware of the legal aspects of their arrangement, such as liabilities to third persons, rights in property, the taxes, and the probable consequences if either

should die. Throughout their working relation they will operate under some kind of legal arrangement even if no thought has been given to the fact.

Different kinds of agreements or types of legal arrangements are described on pages 1 to 7. This information is included only for guidance. State laws vary and the applicable laws are subject to change. So this information should be thought of as only suggesting the things to be considered in drawing up an agreement. A lawyer should be consulted in planning and drawing up the agreement.

Providing for termination of agreement.—It is well to plan at the beginning how the agreement may be ended in an orderly way.

How the interests of each cooperator are to be handled if one of the cooperators dies should be part of the agreement. If it is decided that the surviving party should continue to operate the farm, provision should be made for this.

A partnership agreement may provide that upon the death of either party the survivor shall be entitled to buy his interest. Or the father's will may provide that the son may buy out the other heirs. It may be difficult for the survivor to do either unless the will also stipulates favorable terms, or unless he is left a considerable amount of money. Life insurance policies may be taken out to provide all or part of the purchase money. But it must be carefully decided who shall own, who shall be beneficiary, and who shall pay the premiums on each policy.

If real property—land and buildings—is owned jointly, the agreement should state exactly how this property is to be handled when the agreement ends. This provision may be what de-